In the Supreme Court of the United States

OCTOBER TERM, 1974

No. 73-2055

SECURITIES INVESTOR PROTECTION CORPORATION, PETITIONER

v.

JAMES C. BARBOUR, AS RECEIVER FOR GUARANTY BOND AND SECURITIES CORPORATION AND GUARANTY BOND COMPANY, INC., AND SECURITIES AND EXCHANGE COMMISSION

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

MEMORANDUM FOR THE SECURITIES AND EXCHANGE COMMISSION

OPINIONS BELOW

The opinion of the court of appeals, reported at 496 F. 2d 145, is printed as Appendix A to the petition for certiorari. The unreported opinion of the district court is printed as Appendix C thereto.

JURISDICTION

The judgment of the court of appeals (Pet. App. B) was entered on April 23, 1974. The petition for a writ of certiorari was filed on July 20, 1974. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

QUESTION PRESENTED

Whether the statutory right of the Securities and Exchange Commission to institute an action to compel the Securities Investor Protection Corporation (SIPC) to discharge its obligations under the Securities Investor Protection Act (the Act) is the exclusive means by which SIPC can be compelled to act, or whether there also exists an implied private cause of action.[1]

STATUTE INVOLVED

Section 7(b) of the Securities Investor Protection Act of 1970[2] provides:

> In the event of the refusal of SIPC to commit its funds or otherwise to act for the protection of customers of any member of SIPC, the Commission may apply to the district court of the United States in which the principal office of SIPC is located for an order requiring SIPC to discharge its obligations under this chapter and for such other relief as the court may deem appropriate to carry out the purposes of this chapter.[3]

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[1]While additional questions have been presented by SIPC in its petition, certain of them are merely "stated to preserve them" (Pet., p. 2, n. 3), and none of them has to be reached at this time if the court agrees with the Commission's position that the statutory right of the Commission is exclusive.

[2]15 U.S.C. 78aaa, *et seq.*

[3]15 U.S.C. 78ggg(b). Other provisions of the Act are set forth in Appendix D to the petition for certiorari.

STATEMENT

The Securities Investor Protection Corporation was created by the Securities Investor Protection Act of 1970 to provide greater protection to the customers of member broker-dealers.[4] Under the Act, SIPC may apply to a court for a decree initiating liquidation proceedings if it determines that a member has failed or is in danger of failing to meet its obligations to its customers and that one or more specified conditions exists.[5] If the application is granted, SIPC is obligated, if necessary, to advance moneys to meet certain customer claims from a fund established and maintained by required contributionss from its members.[6] Should the fund become insufficient for the purposes of the Act, the Securities and Exchange Commission is authorized to make loans to SIPC and to issue notes for this purpose to the Secretary of the Treasury in an aggregate amount not to exceed $1,000,000,000.[7] The Securities and Exchange Commission is also given certain supervisory authority over SIPC, and it is specifically authorized to apply to a district court for an order requiring SIPC to discharge its obligations under the Act.[8]

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[4] 15 U.S.C. 78ccc(a); S. Rep. No. 1218, 91st Cong., 2d Sess., p. 1; H. Rep. No. 1613, 91st Cong., 2d Sess., p. 1.

[5] 15 U.S.C. 78eee(a)(2).

[6] 15 U.S.C. 78fff(f).

[7] 15 U.S.C. 78ddd(g) and (h).

[8] 15 U.S.C. 78ggg.

From June 20, 1962, until after the effective date of the Securities Investor Protection Act on December 30, 1970, Guaranty Bond and Securities Corporation (Guaranty Bond) was a broker-dealer registered with the Securities and Exchange Commission pursuant to Section 15(b) of the Securities Exchange Act of 1934[9] (Pet. App. C, p. C-2). On December 22, 1970, the Commission filed a complaint and moved for a preliminary injunction against Guaranty Bond, alleging, *inter alia*, that Guaranty Bond was and had been in violation of the Commission's "net capital rule"[10] (Pet. App. A, p. A-1).

On January 6, 1971, the district court found that Guaranty Bond had been in violation of the net capital rule for a substantial period of time prior to the filing of the complaint and issued a preliminary injunction against further violations (Pet. App. A, pp. A-1—A-2; Pet. App. C, p. C-1). On January 29, 1971, on the Commission's motion, the court appointed a receiver for Guaranty Bond (Pet. App. C, pp. C-1—C-2).

On March 31, 1972, after the receiver had substantially completed the liquidation of Guaranty Bond, he filed a petition with the district court in the Commission's injunction action asking that SIPC and the Commission be ordered to show cause why SIPC should not be required to intervene in the action and extend the protection of the Act to the customers of the brokerage firm (Pet. App. A, p. A-2). The district court issued the requested order and subsequently filed a Memorandum

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[9]15 U.S.C. 78o(b).

[10]17 C.F.R. 240.15c3-1.

Opinion (Pet. App. C) in which it held: (1) The receiver could maintain an action against SIPC on behalf of the customers of Guaranty Bond (Pet. App. C, pp. C-4—C-5), but (2) the customers of the firm were not entitled to protection under the Act because the evidence demonstrated that the firm was "hopelessly insolvent" prior to the effective date of the Act, and "to grant the requested relief would be a retroactive application of the Act and a clear frustration of legislative intent" (Pet. App. C, pp. C-5—C-7).

The district court stated, however, that Guaranty Bond continued to do business until January 6, 1971, and that it handled 101 transactions between December 30, 1970, the effective date of the Act, and January 6, 1971, the date on which the preliminary injunction was issued (Pet. App. C, p. C-1).

The court of appeals agreed with the district court that the receiver had standing to bring an action seeking the customer protections provided under the Act (Pet. App. A, pp. A-8—A-10), but it reversed the determination that Guaranty Bond's customers were not entitled to protection under the Act in light of the substantial business conducted by Guaranty Bond after the effective date of the Act (Pet. App. A, pp. A-5—A-8).

DISCUSSION

The court of appeals erred in concluding that the receiver of a broker-dealer, who represents the interests of the firm's customers, has an implied right to compel SIPC to file an application to commence liquidation proceedings under the Act. The implication of such a private cause of action is contrary to the principle this Court recently enunciated in *Nat'l R.R. Passenger Corp.* v. *Nat'l Ass'n of R.R. Passengers*, 414 U.S. 453, 458:

"[T]he inference of such a private cause of action not otherwise authorized by the statute must be consistent with the evident legislative intent and, of course, with the effectuation of the purposes intended to be served by the Act." Here, neither the legislative intent nor the purposes of the Act are consistent with such an inference.

The Act contemplates that SIPC will be subject to substantial supervision by the Commission, acting in the public interest; to infer that a receiver representing private investors possesses an enforcement right parallel to the Commission's is inconsistent with the design of the Act. Section 7(b) authorizes the Commission to apply to "the district court of the United States in which the principal office of SIPC is located for an order requiring * * * " SIPC to act. In light of the statutory pattern, this specific language authorizing only the Commission to act against SIPC suggests that Congress intended that to be the exclusive procedure for compelling SIPC to act. *Nat'l R.R. Passenger Corp.* v. *Nat'l Ass'n of R.R. Passengers, supra*; *Botany Worsted Mills* v. *United States*, 278 U.S. 282; *Bohart-McCaslin Ventures, Inc.* v. *Midwestern Securities Corp.*, 352 F. Supp. 937 (N.D. Tex.). Nor does the legislative history of the Act indicate that Congress intended that there be a private right of action against SIPC, in addition to the authority given to the Commission.[11]

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[11]The House Report states only:

> Section 7(b) of the bill provides that, should SIPC refuse to commit its funds or otherwise act for the protection of customers of any member, the Commission could apply to a court for an order requiring SIPC to discharge its obligations under this legislation or for such other relief as the court may deem appropriate to carry out the purposes of the legislation—for example, requiring SIPC to file an application under section 5.

H. Rep. No. 1613, 91st Cong., 2d Sess., p. 22.

Moreover, as SIPC points out in its petition (Pet., p. 14), the public interest, not merely the private interests of customers of a broker-dealer, must be considered in determining whether liquidation proceedings should be commenced in a particular instance. Often, although the bases for such proceedings exist, forbearance may allow time for other viable solutions such as the infusion of new capital, the transfer of accounts to a healthy firm, or the merger, acquisition or self-liquidation of the troubled firm. In addition, sophisticated financial analysis and the application of complicated rules and regulations may be involved in a determination to forbear.

Because of the Commission's responsibilities to regulate broker-dealers under the Securities Exchange Act of 1934[12] and to supervise SIPC under the Securities Investor Protection Act,[13] the Commission, and not a receiver of a broker-dealer, should determine whether SIPC has acted

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[12]15 U.S.C. 78a, *et seq.*

[13]The House Report states:

> Your committee has, however, provided for substantial oversight on the part of the Commission over the conduct of the affairs of SIPC. * * *
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> Your committee, not only directs, but expects the Commission to use its oversight in a vigorous, but fair, manner. Only with the cooperation and coordination between the efforts of the self-regulatory organizations, SIPC and the Commission, can this legislation see its fullest effectiveness.

H. Rep. No. 1613, 91st Cong., 2d Sess., p. 12.

improperly in not instituting liquidation proceedings.[14] A broker-dealer's customer or its representative would rarely consider the public interest in determining whether to bring an action to compel proceedings under the Act. As SIPC points out (Pet., p. 15), such an action might be brought with respect to a firm in weak but not terminal financial condition and as the result of legitimately disputed transactions between the firm and the customer; such an action, because of the attendant unfavorable publicity, could start a fatal run on the firm. Moreover, by bringing an action prematurely a customer might destroy viable alternatives to liquidation proceedings.

CONCLUSION

For the foregoing reasons, the Commission is of the view that the court of appeals erred in holding that the receiver of a broker-dealer has an implied right to compel SIPC to file an application to commence liquidation proceedings under the Act.

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[14]We do not maintain that Congress intended that the protections of the Act might be arbitrarily withheld from customers of an insolvent broker-dealer whose claims cannot otherwise be satisfied. See S. Rep. No. 1218, 91st Cong., 2d Sess., p. 3; H. Rep. No. 1613, 91st Cong., 2d Sess., p. 3. It may be, therefore, that a determination by the Commission not to take action under Section 7(b) would be judicially reviewable for abuse of discretion.

The Commission has had insufficient experience under the Act, however, to have any opinion whether the issue is sufficiently important in the administration of the Act to warrant review by this Court.

Respectfully submitted.

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